

I, Douglas Montague, declare as follows:

1. I am a Principal of Montague DeRose and Associates, LLC (“MDA”). MDA serves as a consultant to the California Department of Water Resources (“the Department” or “DWR”) in connection with the Department’s power purchase program.
2. I have served as either an investment banker or financial advisor to municipal clients primarily in California, Utah, Nevada, Washington and Arizona since 1984. I began my municipal finance career with Lehman Brothers in its New York headquarters in 1984. Over the next nine years, I completed, as financial advisor or underwriter, more than \$22 billion of short term and long-term financings. I joined CS First Boston in 1993 to manage the firm’s Los Angeles public finance office and continued coverage of state and county level issuers. In 1995, I established Montague DeRose and Associates. I have completed a variety of different types of financings including fixed and variable rate, sales tax supported, revenue bonds secured from a variety of revenue sources, certificates of participation, lease revenue bonds, pension obligation bonds, Mello-Roos bonds, single issuer and joint powers authority structures. I received a Bachelor of Arts degree in Business Management from the University of Utah and a Master of Business Administration degree in Finance from the Wharton School of the University of Pennsylvania.
3. MDA is an independent financial advisory firm committed solely to public finance. Founded in 1995, MDA is a California Limited Liability Company. I am a principal and beneficial owner of the company. MDA is a west coast firm, with particular focus in general municipal, utility and transportation finance in the states of California and Washington. The firm has offices in Westlake Village and Walnut Creek, California to serve the advisory needs of its clients. Since its inception, MDA has provided service to dozens of nationally recognized municipal entities, including work related to the issuance of nearly \$18 billion in tax-exempt and taxable debt. In 2001, MDA ranked fourth in the Western States in competitive and negotiated bond sales.
4. Over the past several years, MDA has served, among others, the following federal, state, local and regional clients:
 - County of Los Angeles
 - City and County of San Francisco
 - City of Long Beach
 - City of Tacoma, Washington
 - California State Treasurer’s Office
 - Washington State Treasurer’s Office
 - California Department of Veterans Affairs
 - Washington State Dept. of Transportation
 - California Department of Water Resources

- San Francisco Public Utilities Commission
- City of Pasadena Water and Power
- City of Tacoma Power
- City of San Diego Water
- City of San Diego Wastewater
- San Diego County Water Authority
- U.S. Department of Transportation
- Federal Highway Administration
- Port of Oakland
- San Bernardino County Trans. Authority
- Fresno County Transportation Authority

5. MDA has served as financial advisor to DWR since October 1995. In this capacity, our advisors have assisted the Department with the structuring and sale of eleven series of bonds totaling more than \$1.5 billion. Transactions completed for DWR since 1995 have included both fixed and variable rate issues and current, advance and forward refundings. We also assist the Department with the management of its \$100 million tax-exempt commercial paper note program.
6. As DWR has been required to take on additional responsibilities at the State level to manage the challenges caused by the disruptions in the California power market, MDA's professionals have been called upon to assist the Department with its new power-related activities. In January 2001, our professionals were retained to assist the Department in the securing of performance letters of credit required by power generators who would no longer sell power to the Department because of perceived credit risk. Our professionals were given a deadline of less than 18 hours to secure the first performance letter of credit for the State. Working through the night with the headquarters of a German Bank, we were able to meet this very tight deadline and the State was able to purchase power the next day, avoiding extended rolling blackouts. Over the next several weeks, we were able to secure commitments for nearly \$1 billion in performance letters of credit to backstop the State's power purchases.
7. After the passage of Assembly Bill 1X ("AB1X") on February 1, 2001, Montague DeRose and Associates was retained by the Department as its financial advisor for the implementation of the State's power purchase program, including the issuance of up to \$13.4 billion in Power Supply Revenue Bonds. The firm has played an important role in the negotiation of key agreements with the California Public Utilities Commission (the "Commission"), the preparation of rating agency presentations, the negotiation of a \$4.3 billion bridge loan agreement, and the preparation of bond documents necessary for the sale of the long-term bonds. In addition, our professionals, along with Navigant Consulting Inc., have been responsible for developing a number of the models used by the Department for the forecasting of the "net short" power requirements of the state and determining the revenue requirements submitted to the Commission for purposes of rate setting.

FINANCING COSTS

8. Financing costs include costs and reserves relating to the \$6.2 billion in State General Fund loans, the \$4.3 billion Interim Loan and the approximately \$11.8 billion proposed Power Supply Revenue Bonds.

General Fund Loans

9. From January 2001 through late June 2001, the only source of funding available to the Department for its mandated power purchasing activities was a loan from the State's General Fund. During that period, General Fund advances were made in an amount of \$6.2 billion. Interest on the advances continues to accrue at the interest rate reported for the State's Pooled Money Investment Account for the date of each advance. Given that the Department did not have available to it any other source of financing, the General Fund advances represented its only borrowing alternative. In addition, use of the Pooled Money Investment Account rate as the interest rate is specified by Division 27 of the California Water Code (the "Act"). As such, these borrowing costs were reasonable. The following is a breakdown of the General Fund advances by date, amount and interest rate.

General Fund		
Advance Date	Advance Amount	Interest Rate
1/23/2001	\$ 400,000,000	6.321%
2/5/2001	500,000,000	6.216%
3/9/2001	500,000,000	6.010%
3/19/2001	500,000,000	5.966%
3/21/2001	500,000,000	5.965%
4/17/2001	800,000,000	5.766%
4/20/2001	300,000,000	5.722%
5/9/2001	302,228,909	5.371%
5/15/2001	650,000,000	5.334%
5/18/2001	500,000,000	5.300%
5/23/2001	250,000,000	5.313%
6/6/2001	250,000,000	5.089%
6/20/2001	758,138,000	4.926%
Total	\$ 6,210,366,909	

10. The balance of the January 23, 2001 General Fund Loan was reduced by \$116,300,000 on July 12, 2001 using General Fund monies on hand in the Electric Power Fund. The aggregate principal amount of the General Fund loan outstanding as of the date of this declaration is \$6,094,066,909.

Interim Loan

11. The Department's \$4.3 billion interim loan (the "Interim Loan") had two primary purposes: (1) to relieve the General Fund of the State from the burden of making additional advances to the Electric Power Fund for such power purchases pending issuance of the long-term bonds, thereby taking the first steps toward making the Electric Power Fund self-sufficient and ultimately repaying the General Fund,¹ and (2) to satisfy the condition in many of the Department's Long-Term Power Contracts under which the power supplier would have had an option to terminate the contract unless the Department issued investment grade "bonds" by a certain date.²
12. During the spring and summer of 2001, it became evident that the General Fund's ability to continue to make advances to the Electric Power Fund would be limited due to the rapid deterioration in State tax receipts. In order to assure that the General Fund would have sufficient resources to meet the primary education, health and safety needs of the State's residents, the decision was made to arrange for third party financing for the Electric Power Fund. Without the acquisition of third party financing, there existed a risk that the State's internal resources would be depleted and the Department would have no alternative means of paying for its power procurement operations.
13. Because the Department had not yet completed the negotiation and execution of key agreements with the Commission and the investor owned utilities to establish the mechanics for rate setting and revenue collection, it did not have a security structure in place that would allow it to obtain third party financing through the public sale of investment grade long-term bonds. Instead the Department's third party financing had to be negotiated as a "bridge" loan with the expectation that the loan would be refinanced with long-term bonds when the requisite agreements were in place.
14. In order for the Interim Loan obligations to be investment grade in the judgment of the nationally recognized credit rating agencies, the Department needed to establish that the Electric Power Fund would continue to be viable and self-sufficient, without additional periodic advances from the General Fund, until the Interim Loan could be refinanced through the issuance of long-term bonds.
15. The amount of external borrowing the Department chose to pursue through the Interim Loan was determined in consultation with the State Department of Finance and was based on the need to satisfy not only the Department's expected or "base case" net operating losses through the planned September or October 2001 issuance of long-term bonds, but the potential net operating losses that might be experienced if the power market dysfunctionality continued for an

¹ Water Code Section 80200 requires repayment of the General Fund to be made "as soon as practicable".

² The Department's Interim Loan obligations constituted "bonds" within the meaning of these power contracts and the Act.

extended period of time. At the time the Interim Loan was negotiated and closed in June 2001, average daily power purchase costs had not yet settled down to their late 2001 levels and uncertainty remained as to what costs would be experienced and whether supplies would be adequate in the summer of 2001. In fact, the Department's net operating loss for May 2001, the last full month before the Interim Loan was executed, was in excess of \$1.7 billion. The \$4.3 billion Interim Loan size was, therefore, based on operating losses that might be expected under a "stress" scenario. The Department also took into account that if the sale of the long-term bonds was significantly delayed and net operating losses continued to occur in the Electric Power Fund, it might be difficult to secure additional third-party financing. Another benefit of substantial Electric Power Fund balances would be that they would also provide evidence to power providers in the spot market that the Department was creditworthy. The amount of the Interim Loan was reasonable and was justified for these reasons, even if worst case operating results in the Electric Power Fund did not materialize in the near term.

16. The terms of the Interim Loan were negotiated by the Department at arms' length with the assistance of the State Treasurer's Office and the Department's financing consultants, and such terms were approved by the State Director of Finance and the State Treasurer as required by Water Code Section 80132. As mentioned above, the Interim Loan was intended as a "bridge" loan, not as permanent financing, and its terms were designed to give the Department incentive to complete the long-term bond financing as soon as practicable, while providing adequate compensation to the lenders if the Department's originally intended schedule was not met.
17. The terms of the Interim Loan were negotiated and the loan was executed in an environment of extreme uncertainty. The loan was executed before the Department had successfully completed its first revenue requirement proceeding with the Commission. There was considerable uncertainty and speculation by potential lenders regarding the expected completion date of the proceeding. As mentioned above, compounding lender concerns was the fact that the Department was involved in protracted negotiations with the Commission regarding the formulation of a rate agreement that was needed to serve as the foundation for the issuance of long-term bonds expected to retire the Interim Loan. The private credit rating indications for the Interim Loan that were secured by the Department from the credit rating agencies fell in the low investment grade category, creating additional lender concerns. This backdrop of uncertainty caused many lenders to decide not to participate in the Interim Loan. In fact, of the five securities firms appointed as co-senior managing underwriters for the Department's long-term bonds, only two opted to participate in the loan. Feedback from the lenders who declined to participate was that the loan origination fees and interest provisions were inadequate to compensate them for the risks involved.
18. While the negotiations of the rate agreement and servicing agreements with the Commission and the investor owned utilities, respectively, ended up being more

difficult to complete than originally expected at the time of the execution of the Interim Loan, the Department had no reason to believe that negotiations would not be completed in time to allow the issuance of the long-term bonds in the fall of 2001. In fact, servicing agreements or servicing orders with all three investor owned utilities were executed by September 2001. The only agreement not executed in time to facilitate the sale of long-term bonds in the fall of 2001 was the rate agreement with the Commission. At the time of the execution of the Interim Loan, the Department fully and reasonably expected that the rate agreement would be executed on a timely basis.

19. The following table provides the detailed interest accrual and payment history of the Interim Loan. Also included are its principal payment activity and scheduled future principal and interest payments, assuming the Interim Loan is not retired prior to its maturity. Future interest payments in the schedule are calculated based on the formulas utilizing the current prime lending rate of 4.75 percent.

Interim Loan Cash Flows

Period	Gross Proceeds	Principal Redemptions	Interest Payments	Gross Payments	Less Capitalized Interest Fund Payments	Net Payments
Jun-01	4,300,000,000.00	-	-	-	-	-
Jul-01	-	-	1,260,000.00	1,260,000.00	1,260,000.00	-
Aug-01	-	-	23,810,500.00	23,810,500.00	23,810,500.00	-
Sep-01	-	-	6,944,666.67	6,944,666.67	6,944,666.67	-
Oct-01	-	-	32,345,124.53	32,345,124.53	32,345,124.53	-
Nov-01	-	-	-	-	-	-
Dec-01	-	-	-	-	-	-
Jan-02	-	-	50,849,999.99	50,849,999.99	50,849,999.99	-
Feb-02	-	-	-	-	-	-
Mar-02	-	66,460,661.44	68,421,953.63	134,882,615.07	66,460,661.44	68,421,953.63
Apr-02	-	384,867,212.60	1,602,734.69	386,469,947.29	-	386,469,947.29
May-02	-	-	-	-	-	-
Jun-02	-	-	51,798,909.09	51,798,909.09	-	51,798,909.09
Jul-02	-	384,867,212.60	2,000,782.29	386,867,994.89	-	386,867,994.89
Aug-02	-	-	-	-	-	-
Sep-02	-	-	51,292,782.35	51,292,782.35	-	51,292,782.35
Oct-02	-	384,867,212.60	1,879,522.76	386,746,735.35	-	386,746,735.35
Nov-02	-	-	-	-	-	-
Dec-02	-	-	49,769,129.96	49,769,129.96	-	49,769,129.96
Jan-03	-	384,867,212.60	2,206,396.28	387,073,608.88	-	387,073,608.88
Feb-03	-	-	-	-	-	-
Mar-03	-	-	44,839,666.34	44,839,666.34	-	44,839,666.34
Apr-03	-	384,867,212.60	2,135,222.21	387,002,434.80	-	387,002,434.80
May-03	-	-	-	-	-	-
Jun-03	-	-	38,861,044.17	38,861,044.17	-	38,861,044.17
Jul-03	-	384,867,212.60	2,206,396.28	387,073,608.88	-	387,073,608.88
Aug-03	-	-	-	-	-	-
Sep-03	-	-	32,740,073.84	32,740,073.84	-	32,740,073.84
Oct-03	-	384,867,212.60	2,206,396.28	387,073,608.88	-	387,073,608.88
Nov-03	-	-	-	-	-	-
Dec-03	-	-	26,192,059.07	26,192,059.07	-	26,192,059.07
Jan-04	-	384,867,212.60	2,135,222.21	387,002,434.80	-	387,002,434.80
Feb-04	-	-	-	-	-	-
Mar-04	-	-	19,430,522.08	19,430,522.08	-	19,430,522.08
Apr-04	-	384,867,212.60	2,135,222.21	387,002,434.80	-	387,002,434.80
May-04	-	-	-	-	-	-
Jun-04	-	-	12,953,681.39	12,953,681.39	-	12,953,681.39
Jul-04	-	384,867,212.60	2,135,222.21	387,002,434.80	-	387,002,434.80
Aug-04	-	-	-	-	-	-
Sep-04	-	-	6,548,014.77	6,548,014.77	-	6,548,014.77
Oct-04	-	384,867,212.60	2,064,048.13	386,931,260.73	-	386,931,260.73
	4,300,000,000.00	4,300,000,000.00	540,765,293.41	4,840,765,293.41	181,670,952.63	4,659,094,340.78

20. The Interim Loan has both taxable and tax-exempt components. The blended cost of the Interim Loan to date is 5.85 percent.

Long-Term Bond Costs

21. As described in my July 9, 2002 testimony in the Commission's Bond Charge proceeding (the "Montague Testimony"), the Department's proposed Power Supply Revenue Bonds are being issued to repay the General Fund and the Interim Loan and to fund bond and power-related reserves required by the credit rating agencies as a condition of their credit ratings.
22. The two-part flow of funds (for Bond Charges and Power Charges), other elements of the proposed security for the Bonds, the proposed final maturity of the Bonds and the method for determining the amount of the Bond issue have

been largely determined by the Rate Agreement and the related Summary of Material Terms (including Addenda), each negotiated between the Department on the one hand and the Commission, in effect representing the interests of affected ratepayers, on the other. Sections 1.1, 4.1, 5.1, 6.1, 6.4, 7.6, 7.9 and 7.10 of the Rate Agreement each contains terms that either directly determine or substantially influence elements of the structure of the Bond issue. In addition, Section 7.10 requires ongoing consultation between the Department and the Commission concerning various aspects of the Bonds. The parties to this negotiation regularly sought and received feedback from the credit rating agencies concerning whether elements of the structure that might create costs were necessary to achieve investment grade ratings. The method of sizing the amounts of various reserves and other accounts were an integral part of these negotiations. The process of development of the financing structure demonstrates, as confirmed by the Montague Testimony, that the proposed structure of the security for the Bonds, including the amounts of the proposed reserves, is reasonable.

23. Similarly, the projected amount of the Bond issue has been determined by calculating the smallest amount that would achieve the purposes of the financing (repaying the General Fund and the Interim Loan) while funding the reserves and other accounts at their respective minimums described by the Summary of Material Terms and paying reasonable costs of issuance. As a result, the projected amount of the Bond issue is reasonable.
24. The projected carrying costs of the Bonds, costs of issuance and other Bond-Related Costs (including interest on the Bonds, various credit enhancement and liquidity facility costs and variable rate hedging costs) have been determined by the Department on the basis of advice from the professionals of the financing team assembled by the Department and the State Treasurer's Office. Ultimately, many of these costs will be negotiated through the State Treasurer's Office as agent for the sale of state bonds and will be determined by financial market forces as the Bonds are sold and/or remarketed. To the extent that actual costs are different from those projected, the Department will take any surplus or shortfall into account in establishing its future revenue requirements. These projected Bond-Related Costs are, therefore, reasonable.

I declare under penalty of perjury that the forgoing is true and correct. Executed on August 9, 2002 at Westlake Village, California.

Douglas Montague